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President's Own Report Reveals Fundamental Problems with Social Security Privatization

February 24, 2004

Dear Colleague:

As you know, the Administration recently released the *Economic Report of the President*. There has been considerable criticism of the report for a number of reasons, including the unrealistic projection of job growth in the coming year and the disregard for the impact of outsourcing on American workers, among others.

What has gotten less attention however, is the Social Security chapter of the report. This chapter highlights a number of fundamental problems with the privatization of Social Security, as well as several contradictions regarding the President's plans to finance such a proposal. We would like to draw your attention to four particular items within the chapter:

Cutting Benefits is a Key Goal of Social Security Reform. The report clearly states that one of two key goals of the President's Social Security reform plan is cutting Social Security benefits. (The other goal is creating private accounts.) This is an important revelation, because the President's five principles for Social Security reform do not include any mention of cutting benefits. In addition, when explaining why privatizing Social Security is a desirable policy, neither the President nor the many other advocates of privatization acknowledge their goal of cutting Social Security benefits.

Current Workers Have Little to Gain From Privatization. The report further reveals that "much of the benefit of advanced funding...occurs outside of the 75-year projection period." In other words, privatization is a reform whose alleged benefits won't be felt until after everyone now paying into the system is dead.

Debt Will Explode Under Privatization. The report presents the effects on public debt of Social Security Reform Model 2, as developed by the President's 2001 Social Security privatization commission. The analysis shows a breathtaking increase in the public debt,

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reaching a peak increase of 24 percent of GDP. The report projects that privatization would cause the level of federal debt to be higher for *nearly 60 years.* This is the same period during which the federal budget -- and our entire economy -- will already be challenged by the need to finance retirement and health benefits for a larger aged population. Whether the transition costs are borrowed, or financed by tax increases or spending cuts, privatization will impose an additional, substantial, and lengthy strain on the federal budget at the time that other commitments must be met.

Report Reveals Need for Tax Increases or Benefit Cuts for Current Retirees. The report states, "The only desirable way to restore solvency is to do so without continued reliance on general revenues." However, the plan analyzed in the report requires extensive and costly general revenue transfers, lasting for more than 30 years. This is inconsistent with the report's stated desire to avoid reliance on general revenues. Moreover, the plan's reliance on general revenues highlights the fact that the diversion of Trust Fund monies to personal accounts creates a *new* deficit in the Trust Fund. In order to lessen his plan's reliance on general revenues, the President will need to either reduce benefits to current and near retirees, or increase Social Security taxes, or both.

These issues all point to a fundamental problem. The President has been advocating Social Security privatization for four years now, but has not provided a specific plan for executing his vision. Privatization has many risks and tradeoffs, but the debate so far has done little to illuminate them. The only way for the American public to understand the tradeoffs involved in the President's desired reform of Social Security is for him to send his own, specific proposal to the Congress for debate. Only then can the nation make an informed choice about whether to pursue the path of privatizing Social Security.

If you have questions or need additional information, please do not hesitate to contact our staff, Kathryn Olson at 5-4021 or Andrea Palm at 5-7163.

Sincerely,

Charles B. Rangel
Ranking Democrat

Robert T. Matsui
Ranking Democrat
Subcommittee on Social Security